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The Manufacturers Hanover
Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

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Despite Some Potholes . . .

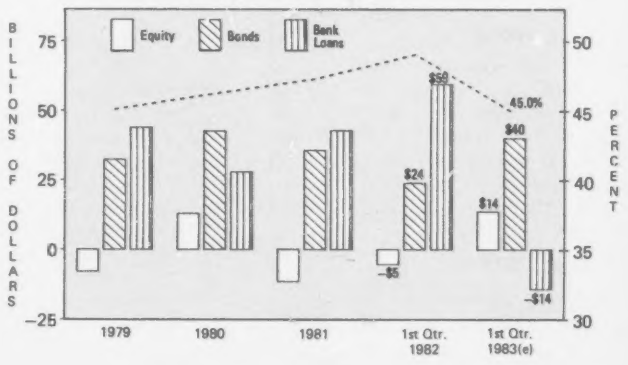
Although the Federal Reserve has repeatedly warned that trends in the M1 money supply are being severely distorted by shifting public liquidity preferences, not to mention financial deregulation and deposit innovation, the financial markets have tended to disregard such advice. Thus, when the nation's basic money supply took an unexpectedly large jump during the first week of May, the response of the credit markets was all-too-predictable: Securities prices tumbled, and yields rose accordingly. This stemmed from the widespread belief among traders and investors alike that with M1 growth accelerating, monetary ease would be put on hold, and prospects for additional interest rate declines anytime soon were remote. What is more, if money supply growth remains robust throughout May, market sentiment will undoubtedly continue to deteriorate. But is such negativism truly warranted?

The answer is—not necessarily. The recent jump in M1 has masked the emergence of a variety of economic and financial developments which suggest that the decline in interest rates might not be over. These include a pronounced slowing of both M2 and M3 growth, the ongoing slump of short-term business credit demands and the persistence of exceptionally low rates of inflation, all of which augur well for further monetary policy flexibility and lower interest rates.

Take money supply growth, for example. To be sure, the $4 billion M1 gain during the first week in May adversely affected market sentiment. But even with this increase, the slowing of M1 growth in recent weeks has been substantial. Indeed, the M1 money supply fell $1.3 billion in April, the first monthly decline since October, 1981. This, of course, represents a welcome reversal of the rates of rise in excess of 20 per cent being recorded earlier this year, when the funds shifts associated with deposit innovation were in full swing. But even more important than this has been the slowing of the growth of the broader money supply measures, a development almost totally eclipsed by the spurt in M1 growth.

In April, the M2 money supply—the aggregate to watch in 1983, according to no less of an authority than Fed Chairman Paul A. Volcker—grew by a modest $5.4 billion, well below the average, $35.6 billion monthly rise which occurred during the first quarter of this year. This placed its year-to-date growth almost $4 billion below 1983's seven per cent *lower* growth target boundary. So, too,

SELECTED SOURCES OF U.S. NONFINANCIAL CORPORATE EXTERNAL FINANCE (BAR) VS. SHORT-TERM LIABILITIES AS A % OF TOTAL (DOT)
(Net change in amounts outstanding; quarterly data at seasonally adjusted annual rates)



year-to-date M3 growth has not been unduly rapid; the $9 billion April gain put the growth of this aggregate not far from the midpoint of its 1983 target boundaries. Thus, if M1 money supply developments might cause the Fed to hesitate before initiating any further moves toward monetary ease, recent M2 and M3 trends do not. Indeed, if the growth of M2 remains below its lower growth target boundary for too long, it may actually hasten an overt easing move.

. . . The Economy Remains On The Road . . .

If money supply developments are not as ominous as a first glance suggests, trends in short-term business credit demands are even more encouraging. Here, too, the emergence of a positive, credit market fundamental has been lost in the M1 fog. The fact is that slumping loan demands, together with strong

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deposit inflows at the nation's commercial banks, have substantially eased pressures in the money markets. This reflects the typical pattern of post-recession corporate finance in which improving cash flows, diminished capital outlays for plant, equipment and inventories and the funding of short-term debt in the long-term markets all combine to keep short-term credit demands quite weak (Financial Digest—March 25, 1983).

While the fading of short-term business credit demands reflects, to be sure, the funding of short-term debt in the bond markets, it is also indicative of something else: namely, the increasing importance of equity finance. Not since 1975 has stock financing played such a major role in the corporate funding process; net new stock issues accounted for approximately one-third of all external funds raised by U.S. nonfinancial corporations in the first quarter of this year.

This compares with an equity-to-external finance ratio of less than five per cent in all of 1982, and represents a development which has tended to dampen credit market pressures in general. And, along with the window of opportunity existing in the bond market, the repair of the badly worn corporate balance sheets has begun in earnest. Both relative maturity and equity ratios are being restored to some semblance of health; the ratio of short-term to total liabilities, for example, may dip to 45 per cent this year from almost 49 per cent last year—the

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 5/11/83	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	146.966	– 2.046	+ 9.295
Loans to Depository Inst.	.709	– .219	– .408
Float	2.095	– .181	– .039
Total Reserve Bank Credit	159.436	– 2.799	+ 8.733
Treasury Deposits with Federal Reserve Banks	3.812	– 2.041	– .882
Currency Outside Banks	140.367	+ 1.298	+11.518
Member Bank Reserves:			
Required	37.568	– 1.376	– 1.326
Excess (Deficiency)	.336	– .270	+ .072
Total Reserves Held	37.904	– 1.646	– 1.254
Net Free Reserves	.224	– .048	+ .667
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	109.971	– .910	+19.442
Monetary Aggregates †		% Change Since Three Months Ago*	% Change Since Year Ago
M1	506.9	+ 11.1‡	+ 10.7‡
M2 (April '83)	2,072.6	+ 12.8	+ 12.9
M3 (April '83)	2,453.7	+ 8.7	+ 10.3
Domestic Nonfinancial Debt (4th Q'82)	4,745.6	+ 10.2	+ 9.2

†Seasonally adjusted.

*Seasonally adjusted annual rate.
‡Four-week moving average.

New York Money Market

Offering Rates 5/20/83	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	7.90%	8.00%	8.05%
* Federal Agencies	8.45	8.50	8.70
* Project Notes—Taxfree (46% Taxable Equivalent)	8.80	9.63	10.37
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	8.65	8.80	9.35

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	8.38%	Jun.	8.50%
15- 29 days	8.38	Jul.	8.50
30- 59 days	8.38	Aug.	8.50
60- 89 days	8.38	Sep.	8.50
90-179 days	8.38	Oct.	8.50
180-239 days	8.38	Nov.	8.45
240-270 days	8.38		

‡Industrial Paper—Prime			
30- 89 days	8.40%	†Federal Funds Effective Rate	8.68%
90-120 days	8.40		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'83	$ 3,171	$ 3,108	$ 2,996
Gross National Product (1972 Dollars)*	1st Q'83	$ 1,486	$ 1,477	$ 1,471
Percent Change, Annual Rate	1st Q'83	2.5	– 1.1	– 5.1
Change in Consumer Prices (new series)*	Mar '83	1.2%	– 2.4%	0.0%
Change in Producer Prices*	Apr '83	– 1.2%	– 1.2%	1.2%
Civilian Employment (Thousands of Persons) †	Apr '83	99,458	99,103	99,484
Unemployment as % of Civilian Labor Force †	Apr '83	10.2%	10.3%	9.3%
Personal Income*	Apr '83n	$ 2,679	$ 2,659	$ 2,536
Leading Indicators Composite Index (1967=100) †	Mar '83	149.8	147.6	134.7
Industrial Production Index (1967=100) †	Apr '83	142.6	139.7	140.2
Net Change in Consumer Installment Credit †	Mar '83	$ 2.58	$ 0.74	$ 0.63
U.S. Merchandise Trade Balance †	Mar '83	–$ 3.63	–$ 3.58	–$ 2.43
Plant and Equipment Expenditures*	2nd Q'83	$302.20(a)	$302.25(a)	$323.22
Private Housing Starts (Thousands of Units)*	Apr '83n	1,490	1,627	911
New Construction Expenditures*	Mar '83	$ 245.4	$ 249.3	$ 224.6
Total Business Inventories †	Mar '83	$ 502.9	$ 508.5	$ 521.2
Total Business Sales †	Mar '83	$ 346.0	$ 339.8	$ 344.4

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. a-Anticipated.

largest year-over-year decline on record (see chart on page 1).

. . . To Lower Interest Rates

One by-product of this is that with bank loan demand softening, yet deposit inflows running at record levels due, in large part, to the exceptional popularity of money market deposit accounts, the differential between bank and Federal government borrowing costs has just about evaporated. For with the volume of certificates of deposit outstanding declining by $40 billion, or 12 per cent since the beginning of December, and Treasury borrowings soaring, the spread between three-month CDs and three-month Treasury bill rates has averaged less than 40 basis points over the past three months, a huge decline when compared with the almost three percentage point spread which existed last September.

Finally, the most important reason for expecting both monetary policy flexibility and lower interest rates in coming months is the persistence of exceptionally low rates of inflation—and the scaling back of inflation expectations among financial market participants. Wage compensation has risen by less than six per cent over the past year, while major collective bargaining settlements in private industry during the first quarter of 1983 resulted in a 1.4 per cent decline in the average wage adjustment during the first contract year—the first negative adjustment in the 15-year history of this series.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (5/4/83)	97,180	– 2,533	–35,092
New York City (5/4/83)	23,774	– 1,284	– 9,720
Commercial Paper (5/4/83)	171,396	+ 1,907	– 3,463*

*Series redefined: Data prior to December 1, 1982, are not strictly comparable to the data reported after that date.

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/4/83)	216,333	+ 1,683	+ 7,614
New York City (5/4/83)	58,284	+ 408	– 674

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/4/83)	503,351	+ 3,610	+16,564
New York City (5/4/83)	116,096	+ 1,644	+ 2,817

Financial Markets

	Friday 5/20/83	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills*	8.60%	+ .20	– 3.20
180-Day Bills†	8.83	+ .23	– 3.65
Longest Bills†	9.10	+ .30	– 3.81
Recent Issues:			
9 1/2s 4/30/85	9.70	+ .28	
10 1/4s 3/31/87	10.10	+ .35	
10 1/8s 5/15/93	10.62	+ .34	
10 3/8s 11/15/12	10.77	+ .34	
Municipals:			
Bond Buyer–20 Bond Index* (5/19/83)	9.29%	+ .43	– 2.67
Blue List Total ($ Million)	$1,476	– $ 7	– $ 334
30-Day Visible Supply ($ Million)	$4,314	– $246	+ $2,654
Total	$5,790	– $253	+ $2,320
Corporates:			
Moody's Aa Composite (5/19/83)	12.03%	+ .21	– 2.76
30-Day Visible Supply ($ Million)	$1,115	– $109	– $1,083
Stocks:			
Dow-Jones Averages:			
Industrials	1,189.92	– 28.83	+ 354.02
Transportation	539.62	– 8.27	+ 206.06
Utilities	128.88	– .73	+ 15.10
65 Stocks	470.12	– 8.94	+ 141.76
Standard and Poor's 500 Stocks	162.14	– 2.76	+ 47.25
N.Y.S.E. Composite Index	93.71	– 1.36	+ 27.45
N.Y.S.E. Avg. Daily Vol. for Week (000's)	82,496	–10,486	+ 35,028

* 46% Taxable equivalent 17.20%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 5/20/83	Week Ago
Overnight	8.75%	8.75%
1 month	8.94	8.88
3 month	9.13	8.94
6 month	9.25	9.00
1 year	9.38	9.19
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	10.95%	11.15%
Long Term (7 to 15 yrs.)	11.05	11.25

FOREIGN EXCHANGE SPOT RATES

New York Opening (5/20/83)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02023	49.44
Canada	.8116	1.2322
Denmark	.1133	8.8250
France	.1345	7.4375
Germany	.4040	2.4755
Italy	.0006790	1472.80
Japan	.004276	233.88
Mexico	.006711	149.00
Netherlands	.3597	2.7800
Switzerland	.4837	2.0675
U.K.	1.5563	.6425

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